Lynn Palmer

Mr. Speice

ISM I

9 March 2018

Mentor Visit Assessment I

Mentor: Patrick Van Ooteghem and Richard Rogers

Profession/Title: Managing Directors

Location: 5910 N Central Expy # 1470, Dallas, TX 75206

Date: February 20th, 2018

Time: 10:00 AM to 4:00 PM

During my second mentor visit, I focused on getting a few projects started with my mentor and continued my work with the Intelligent Investor. When I first got to the office, I was assigned to provide a rationale for my acquisition of PayPal after their spinoff with eBay. Researching more current data about PayPal and reading various documents like their earnings calls allowed me to get a more up-to-date opinion on PayPal and brought my attention to two major pieces of information that I have missed since the last time I evaluated Paypal: their very high growth and small business loans through eBay.

The first problem that I tackled was the high growth that was reported through their most recent earnings call (Q4 of 2017). In the type of businesses that I typically invest in, 10-15% growth is considered “normal”. Surprisingly, PayPal was growing some measurements (like active customer accounts) by over 50%. Even though they had a very atypical situation for high growth being a very established and focused technology and finance company, they were able to

produce these tremendous figures. Naturally, I regarded this with skepticism. For most established businesses, growth rates that reach over 20% are cause for concern for things like accounting fraud and massive amounts of debt. This brought me to examine the strategic position of the company since their 2015 IPO, where I discovered the reason behind this growth. As PayPal established itself as a newly-independent company, they went on a massive spree of acquisitions, focusing on extremely small tech startups that eventually caused the massive growth that we are seeing today. This genius move by President Dan Schulman enabled PayPal to get the specialized technology that these small startups created at an extremely low price, and this technology is now being used in large volumes of activity through PayPal. This discovery allowed me to gain more information about strategies that companies, especially new startups, can use to produce extremely high returns later.

The second discovery that I made through my research into PayPal was the small business loans that they have been slowly expanding since the spinoff. These were some of the most interesting loans that I have encountered so far because of the method of paying it off. First, PayPal has an inherent advantage in offering small business loans to eBay sellers. Because PayPal has long been the exclusive method of payment for eBay, they can obtain all of the seller's information at no cost, allowing them to very quickly and easily determine how likely a seller is to pay off their loan. This allows them to approve loans in a matter of minutes, making it easier for sellers to obtain loans. PayPal's ability to approve these typically small and quick loans allows them to charge a higher annual percentage rate (APR) than typical bank loans, sometimes charging over 20% APR. Finally, to make sure that sellers pay off their loans, PayPal has created one more layer of security: automatically taking payments out from each sale that the seller

finalizes. For example, PayPal may take out 5% of the sales from a seller that took out a $10,000 loan with a 20% APR to be paid off over the next twelve months. By doing this, the loan begins to be paid off as soon as it is issued.

As my mentor and I worked through these interesting characteristics of PayPal during the intern meeting, we turned toward the topic of pension funds within large corporations. From our discussion, I learned from my mentor that pension funds can be an accurate indicator of the trustworthiness of management. All companies publish their anticipated rate of return that they will earn on their pensions. Because of this, a projected return that is much higher than the discount on T-bills (which is what most pensions are made up of) could indicate that management is very aggressive and overconfident while a lower discount indicates more realistic and down-to-earth management. Knowing this, I will now look at the pension funds of both PayPal and the other companies that I value to anticipate the general sentiment and character of the management team.

Overall, I discovered many things about both companies that I am familiar with and concepts that are foreign. I will be able to apply these improved skills of research and analysis throughout my final product, and I hope I will be able to further expand on these concepts during the rest of my mentor visits.

Meeting 2/20 Notes

Pension
- Use Total Obligations
- Projected return of pension — honest management (too high compared to T bills?)
  - If too high... aggressive and unreliable management
  - If too low...
- Look at some pensions...

PYPL Reasoning

Interested by the EBY PYPL spinoff
- At that point, basically two separate firms
- PYPL's earnings were consolidated into EBY but you could tell PYPL was growing faster
  - Could be suitable for more than just EBY

Online payments were taking off

Directly after spinoff - acquisition of Braintree, Venmo, a few smaller ones
- Got all of the startup technology, eliminating smaller competitors rather than going after the large ones
- Now, rapid breadth expansion because they have a well developed platform
  - Always aggressive, founded by Elon Musk/Peter Thiel

Breadth: Have both AliPay and Baidu (99% of Chinese online retail), cross platform beats out things like ApplePay

PayPal and Ebay now: Ayden
- Still have a relationship until 2023, probably get more information about it once that date gets closer
- At that point Ebay will be less than 10% of their revenues, excluding acquisitions